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IN THE

Supreme Court of the United States

OCTOBER TERM, 1969

No. .....

IN THE MATTER OF

THE CENTRAL RAILROAD COMPANY OF NEW JERSEY,

Debtor.

JOHN E. FARRELL, TRUSTEE OF THE PROPERTY OF THE CENTRAL RAILROAD COMPANY OF NEW JERSEY,

Petitioner,

vs.

MANUFACTURERS HANOVER TRUST COMPANY, TRUSTEE OF THE GENERAL MORTGAGE WHICH SECURES THE GENERAL MORTGAGE BONDS OF THE DEBTOR,

Respondent.

BRIEF IN OPPOSITION TO A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Respondent Manufacturers Hanover Trust Company, Indenture Trustee of the debtor railroad's general mortgage respectfully opposes the allowance of certiorari in this matter.

1. *Bondholders' Senior Right to Mortgaged Assets.* It is essential to bear in mind the true nature of the fund as to which competing claims or uses are asserted herein. Rules of priority do not exist *in vacuo* and are not wholly uniform as among different sorts of funds.

The case *sub judice* involves mortgaged property, i.e. the cash proceeds of mortgaged real estate previously sold by permission of the District Court. The account in which the cash was held was established by an order of the District Court under terms which preserved the "corpus" nature of the cash. As the District Court wrote (App. A, p. 2a), the proceeds

> "are normally withdrawable by the Trustee to pay for needed additions or betterments to, or the purchase of, other real property, which would be or become subject to the lien of the General Mortgage."

The question, then, is whether part of the mortgaged corpus may be dissipated—not reinvested—in operating expenses. The Court of Appeals epitomized the problem thus (App. B, p. 12a):

> "The court's order leaves the Indenture Trustee with a bridge of uncertain value and a cash fund diminished by $408,000."

Not only is removal of a structure not a preservation or enhancement of it, but the costs of removal are classified as operating expenses by the Interstate Commerce Commission (App. B, p. 11a, fn. 6).

The cases cited by the petitioner Reorganization Trustee, therefore, neither conflict with the Court of Appeal's holding nor require its review by this Court. Three of them deal with the quite different questions of priority as to operating revenues or a special statutory priority of payment not herein involved. Expenses of administration may indeed "be given priority over the mortgage liens" (Petition for Writ, p. 8), *but only as to income.* Thus, in *In Re Chicago, R. I. & P. Ry Co.*, 90 F. 2d 312, (7th Cir., 1937), cert. den. 302 U.S. 717, 58 S. Ct. 37 (1937), the fund in dis-

pute was repeatedly described as "income". *Central Hanover Bank & Trust Co.* v. *Williams,* 95 F. 2d 210 (8th Cir., 1938) merely decided the constitutionality of Section 77 (n) of the Bankruptcy Act, 11 U. S. C. A. §205, by which injured employees of the debtor railroad are granted a special priority. It is not clear from the opinion, moreover, what source of funds was allowed to be applied to the claimant's $15,000 judgment; so that the relevance of that case is doubly questionable. *Thompson* v. *Siratt,* 95 F. 2d 214 (8th Cir., 1938), a contemporaneous decision of the same Circuit Court, is exactly the same as to issue and holding. The Petitioner's fourth case, *Ecker* v. *Western Pacific R. Corp.,* 318 U.S. 448, 454, 63 S. Ct. 692, 714, 87 L. ed. 892, 940 (1943) dealt (in context) merely with the ranking of accrued and unpaid "current liabilities, trustees' obligations and reorganization expenses" in a plan of reorganization.

On the contrary, the Court of Appeal's determination here in issue is wholly consistent with prior decisions that the mortgaged corpus may be reinvested in substitute collateral or altered as form, but is not to be dissipated in operations absent some very special reason. Thus, in *In re New York, New Haven and Hartford Railroad Co.,* 289 F. Supp. 451 (D. Conn., 1968), the withdrawal and disbursement of specific mortgaged funds was expressly conditioned upon the replacement of such funds by substitute collateral of equivalent value. This requirement does not appear in the opinion but was made known to the Court of Appeals in this case by exhibiting the actual text of the order entered by Judge Anderson (App. B, p. 11a, fn. 7). Judge Anderson wrote, 289 F. Supp. at 450:

> "In addition, no funds now in the registry of the court, held in lieu of mortgaged property which has been sold, will be used to pay operating losses."

So too, in the other cases cited by the Court of Appeals, there was a substitution (therefore a preservation) of collateral, such as real property facilities, *In re New York, New Haven and Hartford Railroad,* No. 30226 (D. Conn., Dec. 7, 1961), or new railroad cars, *Harding* v. *Stichman,* 240 F. 2d 289 (2d Cir., 1957), or fabricated inventory, *Reconstruction Finance Corp.* v. *Kaplan,* 185 F. 2d 791 (1st Cir., 1950). Even in the trial court's determination, reversed, in *In re Third Avenue Transit Corp.,* 198 F. 2d 703 (2d Cir., 1952), an interest-bearing trustee's certificate was offered in replacement of mortgaged cash.

Contrary to Petitioner's suggestion (Petition for Writ, p. 8), the Court of Appeals did not rely particularly heavily upon *In re New York, New Haven & Hartford Railroad,* 278 F. Supp. 592 (D. Conn. 1967); but in any event Judge Anderson's discussion therein of the relative seniority of bondholders over six-month claimants is illustrative, by analogy, to the present question.

The respondent Indenture Trustee Manufacturers Hanover Trust Company did not press in the Court of Appeals for immediate repayment or substitution of the collateral (App. B, pp. 14a-15a). It submits, however, that the protection afforded it by the Court of Appeal's mandate—that is, a specific obligation on the part of the petitioner Reorganization Trustee to repay the sum in the future under the supervision of the District Court and, in effect, a recognition of such obligation as being a prior claim in the nature of a mortgaged asset (App. B, p. 16a)—is thoroughly consistent with the protections afforded bondholders in the cases discussed above.

2. *Allowance of "Interest" upon Reimbursement.* Petitioner Reorganization Trustee also complains of the requirement for interest upon repayment into the mortgaged

fund (Petition for Writ, p. 11; and see App. B, pp. 16a-17a). There is no occasion now for this Court to resolve any "dispute" over whether interest normally accruing on the mortgaged fund belongs to the Reorganization Trustee or the bondholders, since the Court of Appeals' requirement was in the nature of a penalty or an equitable remedy fashioned to encourage compliance with its mandate—clearly a matter within its discretion—and did not project the legal question of the ownership of interest in the ordinary sense.

CONCLUSION

The Court of Appeal's determination in question is consistent with prior decisional law, and there is no occasion for this Court to review it.

Respectfully Submitted,

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Newark, New Jersey
May 19, 1970